EDUCATIONAL AID 8

Ways Farmers Do Business

FARMER COOPERATIVE SERVICE
U.S. DEPARTMENT OF AGRICULTURE

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Farmer Cooperative Service conducts research; advises directly with cooperative leaders and others; promotes cooperative organization and development through other Federal and State agencies; and publishes results of its research, issues *News for Farmer Cooperatives,* and other educational material.

This work is aimed (1) to help farmers get better prices for their products and reduce operating expenses, (2) to help rural and small-town residents use cooperatives to develop rural resources, (3) to help these cooperatives expand their services and operate more efficiently, and (4) to help all Americans understand the work of these cooperatives.

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The following material has been prepared as a guide for a team demonstration. As much as possible the two team members should tell the story in their own words, based on the written material. However, the team may brighten their presentation by adding supplementary information, such as reference to cooperatives in their own neighborhood with which their audience may be acquainted.

The caption, chart, and tables may be used to construct a flannelgraph or blackboard presentation. Experience of those who have used such visual aids to illustrate the talk has been good. Listeners are apt to be much more interested and attentive when the talk is backed up with visual aids. And they tend to remember better what they have heard if hearing is coupled with seeing.

SPEAKER A

To be successful, a farmer must not only be an efficient producer--he must also be a good businessman. Today we're going to look into the three main kinds of firms through which or with which the farmer does business.

SPEAKER B

In recent years, the business side of farming has become more and more important. Here's why--

Today, farmers put more money into production than they used to. They use more fertilizer and they buy practically all of it. They spend more on tractors and machinery. They buy more seed, pesticides, feed and feed supplements. They farm on a larger scale.

SPEAKER A

All of which means that farmers are doing more business with others and away from the farm than they used to. And their success depends on carrying out each transaction--whether it is buying or selling--in the most profitable way.

SPEAKER B

Farmers can do business with or through one or more of the three major types of business firms which operate in our American private enterprise system.

These three types are:

1. Individual ownership
2. Partnership
3. Corporation
    a. Regular
    b. Cooperative

Note that the cooperative is a corporation also--but one of a special kind.

SPEAKER A

We will emphasize cooperatives in this demonstration because this type of firm is one that many farmers can use to advantage.

Farms are relatively small business units when compared to many of our businesses today. This can be a disadvantage when it comes to doing business. Because they do business in relatively small quantities on this basis of comparison, most farmers still must buy supplies at retail and sell products at wholesale.

Thousands of farmers have overcome this difficulty by joining with other farmers in cooperatives that handle their off-farm business. Today, farmers sell about a fourth of all their products and buy about a fifth of all their supplies through cooperatives.

SPEAKER B

Now let's look at the three kinds of business firms more closely and see how they differ.

We won't spend much time on numbers 1 and 2--individual ownerships and partnerships--because you quite likely are familiar with these. For example, you all know that the individual farmer, doing business by himself, buying his supplies and selling what he produces as best he can, is operating on an individual ownership basis. And if he is doing this business with someone else jointly, such as his son, this is an example of a partnership.

We will look into regular corporations and cooperatives in more detail. They are more complex in makeup and operation. And you have to examine them closely to see how they differ.

Individually Owned Business

SPEAKER A

The individually owned business is the oldest and by far the commonest type of firm.

In a business of this type, one person puts up all the money for the operation--his own or money he has borrowed. He makes all the decisions. Often he does a large part of the work himself, although he may hire others to help him. All the profits of the business are his. Similarly, he must take all losses.

Most farm businesses are individually owned, because experience has shown that this has many advantages in farming, particularly in production.

Partnerships

SPEAKER B

In a partnership, two or more persons pool their resources in one enterprise. They do not necessarily contribute equal amounts of each resource. One may put in more money, for example--another more time and labor.

The main advantage of a partnership over single ownership is that it is possible to get more resources into a business. It also gives each partner use of resources other than his own.

A young man, for example, might want to go into farming--but not have the amount of capital needed to start. An older farmer may have the land, livestock, and equipment, but no longer possess the energy needed to attend to all the day-to-day details. The two may combine their resources into a farm partnership--to their mutual advantage.

A main limitation of a partnership is that each partner is individually responsible for all of the firm's debts. If it loses money, a partner can lose more money than he has put in.

Another disadvantage is that when one of the partners dies or retires, the others must make a settlement. Often the surviving partner(s) must buy the deceased partner's share, unless there is a written agreement or will decreeing otherwise. This is why it is important that all partnership agreements be in writing, and that each partner prepare a will.

Regular Corporations and Cooperatives

SPEAKER A

Now for number 3--the regular corporation and the cooperative. As we have mentioned, cooperatives are usually a special kind of corporation. Those that are not incorporated are roughly the same as partnerships.

So, just what is a corporation?

SPEAKER B

A corporation is a group of persons empowered by law to act as a single person. Those who want to form a corporation must get government permission to do so--usually from a State government. The State gives them this permission in a paper called a charter. After the organization gets the charter, it is said to be incorporated.

In order to get a charter, those who want to organize the corporation must file articles of incorporation. This is a statement of the kind and scope of business the corporation will do. And it must be drawn up to conform with State laws. All States have separate laws governing business corporations, both cooperatives and ordinary corporations, although a few States do not have laws specifically relating to cooperatives.

SPEAKER A

A corporation has three main advantages as a way of doing business.

1. It can have many owners (stockholders); therefore it is possible to get a lot of money into one business.
2. Normally each stockholder risks only the amount of money he agrees to invest through purchase of shares.
3. Changes in ownership do not interrupt the business. If stockholders die or sell out, new owners take their places and the business operation goes right on.

SPEAKER B

Both the regular corporation and the cooperative corporation have these three advantages.

Now let's see the differences in the two kinds of coperations.

These differences are summed up here in figure 1.

Briefly, a farmer cooperative is a business operated at cost and organized to do things the farmer needs to have done. It may sell his products, for example, buy his supplies, or obtain some special service for him--such as electricity or telephone service or irrigation.

The farmer members own the cooperative, run it at cost, and use it. The cooperative's owners and its customers are one and the same.

On the other hand, a regular corporation is in business to make money for its owners (stockholders). Its owners may not even be customers of the business. If they are, they may make up only a small percentage of the customers.

Figure 1

COMPARISON OF FOUR METHODS OF DOING BUSINESS UNDER PRIVATE ENTERPRISE

Features compared	Types of business			
	Individual	Partnership	Regular corporation	Cooperative (usually corporation)
1. Who uses the services?	Non-owner customers	Generally non-owner customers	Generally non-owner customers	Chiefly the owner patrons
2. Who owns the business?	The individual	The partners	The stockholders	The member-patrons
3. Who votes?	None necessary	The partners	Common stockholders	The member-patrons [1]
4. How is voting done?	None necessary	Usually by partners' share in capital	By shares of common stock	Usually one-member one-vote
5. Who determines policies?	The individual	The partners	Common stockholders and directors	The member-patrons and directors
6. Are returns on ownership capital limited?	No	No	No	Yes--8% or less (usually less, if any) [1]
7. Who gets the operating proceeds?	The individual	The partners in proportion to interest in business	The stockholders in proportion to stock held	The patrons on a patronage basis [1]

[1] Basic principles of cooperation.

Voting

SPEAKER A

Let's see how these differences show up in operations.

Let's imagine that 10 club members are operating family farms and are owners of a corporation and also members of a cooperative.

Both businesses are performing identical services. They are just operated differently.

First, let's compare how the 10 stockholders would vote in each organization.

In table 1 we have outlined the number of shares and the number of votes for each member. Each corporation has 100 shares of stock and each member has the same amount of stock in both corporations.

SPEAKER B

Note that in the regular corporation each member has as many votes as he has shares. The first three have 51 percent of the votes and can definitely control the organization. It would be the same if one of them had 51 percent of the votes.

This is in accord with recognized control practices in ordinary corporations. The purpose of the business is to earn money for the investors. Those who have the largest investment have the greatest financial interest as well as the most votes. Often they become the key officers.

SPEAKER A

Now look at the votes in the cooperative. Each member generally has one vote. Thus Bates (see table 1) even though he is president with 20 shares of stock has the same vote as Jones who has only 4 shares.

Is this fair? Bates has five times as many shares of stock as Jones and yet they vote the same.

Table 1.--Comparison of the usual methods of voting in ordinary corporations and cooperatives

Stockholder	Ordinary corporation		Cooperative corporation	
	No. shares	No. votes	No. shares	No. votes
James Bates, President	20	20	20	1
John Abrams, Vice President	20	20	20	1
R. H. Harper, Secretary	11	11	11	1
Geo. Brown, Treasurer	10	10	10	1
Richard Allison	9	9	9	1
B. U. Alexander	8	8	8	1
J. H. Butler	7	7	7	1
P. A. Budd	6	6	6	1
Albert Henson	5	5	5	1
R. A. Jones	4	4	4	1
Totals	100	100	100	10

The answer is that the purposes of the two organizations differ. Owner-patrons of the cooperative are interested in providing needed services at cost. They are all equally interested in getting these services. Thus each has an equal share in the votes.

This is the actual method of control used in four out of five cooperatives in the United States. In most of the others, additional votes are permitted according to increased use of the cooperative by the member.

In other words, the basis of voting is the interest of the member in the services of the business rather than in the dollars he has invested in it.

The officers are the same in each business. But in the cooperative all members elected them. In the ordinary corporation they may have elected themselves because they own enough stock to control the voting.

Sharing the Earnings

SPEAKER B

So much for the votes and control. Now let's see how the owners share in the proceeds of these two corporations.

In the ordinary corporation, the job of dividing up the year's proceeds is easy. The company earned $1,000 during the year--which is 10 percent of the total investment. Therefore each member gets 10 percent on his investment. (Go down table 2 and point out what Jones, Brown, and Bates get.)

In the cooperative we have a different picture.

SPEAKER A

The point is that members of a cooperative are paid limited dividends on this investment. To assure patrons of a cooperative

Table 2.--Usual method of distributing operating proceeds among common stockholders of an ordinary corporation [1]

Stockholder	Stock owned	Earnings
James Bates, President	$2,000	$200
John Abrams, Vice President	2,000	200
R. H. Harper, Secretary	1,100	110
Geo. Brown, Treasurer	1,000	100
Richard Allison	900	90
B. U. Alexander	800	80
J. H. Butler	700	70
P. A. Budd	600	60
Albert Henson	500	50
R. A. Jones	400	40
Total	10,000	1,000

[1] Proceeds equal 10 percent of capital investment.

that their services will be provided at cost, the amount of dividends that can be paid on capital is limited by law.

In our State it is______ (check State law for amount). Usually, the top rate the cooperative can pay is also set forth in the association's bylaws. Each year the directors decide just how much is to be paid. This is frequently less than the amount that is actually permitted in the bylaws or the State law.

In our imaginary cooperative the members are paid 5 percent dividends on their capital. Thus Brown gets $50 on his $1,000 investment, Henson $25 on his $500 investment, Bates $100 on his $2,000 investment.

SPEAKER B

The dividends paid to members of the cooperative on their investment are a limited return on capital. Any net margins that may remain <u>after</u> payment of dividends on capital stock are available for distribution on a patronage basis.

SPEAKER A

So the cooperative returns this net margin accordingly to the patrons in the form of patronage refunds.

As you can see, members didn't use the cooperative in the same proportion that they invested in it. All of these together did $50,000 worth of business during the year. However, Bates and Abrams--the big investors--did a little more business than Budd and Jones, the small investors. The cooperative divided the $500 available after all costs and dividends on stock were paid, according to the business each member did with the organization. Brown, who did $5,000 worth of business, gets $50 back. Bates did $6,000 worth of business, so he gets $60.

SPEAKER B

How did the owners come out when their operations in the two types of corporation were compared ? (Refer to table 3, page 11.)

Brown, who had an average investment and did an average amount of business with the cooperative received $100 in each case. Henson, who had a below-average investment and did an

Table 3.--Comparison of the results of distributing operating proceeds among owner-patrons of a cooperative with those of an ordinary corporation [1]

Member-patron	Capital owned	Dividends paid on capital [2]	Patronage volume	Patronage refunds	Total proceeds	Variation from non-coop. method
James Bates, President	$2,000	$100	$6,000	$60	$160	-$40
John Abrams, Vice President	2,000	100	6,000	60	160	-40
R. H. Harper, Secretary	1,100	55	4,000	40	95	-15
Geo. Brown, Treasurer	1,000	50	5,000	50	100	0
Richard Allison	900	45	4,000	40	80	-5
B. U. Alexander	800	40	6,000	60	100	+20
J. H. Butler	700	35	5,000	50	85	+15
P. A. Budd	600	30	5,000	50	80	+20
Albert Henson	500	25	4,000	40	65	+15
R. A. Jones	400	20	5,000	50	70	+30
Total	10,000	500	50,000	500	1,000	

[1] Proceeds equal 10 percent of capital investment.
[2] Five percent.

average amount of business, got $65 in the cooperative example and $50 in the ordinary corporation example. Bates, who had a big investment but who did just a little over an average amount of business with the cooperative, got $40 less from the cooperative than from the corporation.

But it must be remembered that the money returns from the two kinds of businesses do not tell the whole story. All of the cooperative members--in addition to the money they received from the cooperative--also received service at cost. This increased their incomes by saving them money, but most importantly, this service came from a business firm they owned, controlled and used.

And best of all, as cooperative members and owners they received valuable business training as they took part in the activities of their cooperative at the annual meeting and on other occasions.

Other Publications Availabl

Farmer Cooperatives in Our Community. Educational Circular 12. A. W. McKay.

Cooperatives--One of Four Kinds of Business Firms. Educational Aid 7.

The American Private Enterprise System. Educational Aid 5. Oscar R. LeBeau.

The Business Rights to Main Street Under Private Enterprise. Educational Aid 1-G. J. H. Heckman.

Farmer Cooperatives--What They Are and What They Are Not. Reprint 255. Marvin A. Schaars.

A copy of each of these publications may be obtained upon request while a supply is available from--

Farmer Cooperative Service
U.S. Department of Agriculture
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